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Policy Brief.....Proposed Terrorism Reinsurance Compromise
Staff Contact Neil Bradley

AGREEMENT SUMMARY

GENERAL PROGRAM SPECIFICS: Program administered by the Secretary of the Treasury. Program terminates on December 31, 2005

COVERAGE: The program is triggered when a terrorism event causes losses in excess of \$5 million. The Federal Government pay 90% of the of the insured losses that exceed the insured deductible (which increases each year of the program). Under the program the Federal Government covers insured losses up to \$100 billion a year. Insured losses do not include punitive damages and federal payments are reduced by the amount of other federal payments to victims.

FEDERAL RECOUPMENT: The bill requires that combination of insured deductibles, non-Federal payments above insured deductibles and surcharges on policyholders be used to cover the first \$10 billion in insured losses for the first year increasing to \$15 billion in year 3. The government may impose additional surcharges for the recoupment of government payments in excess of the \$10 to \$15 billion figures at its discretion.

TORT AGREEMENT:

	House	Senate	Deal
Punitive Damages	Prohibited	Punitive Damages Permitted (Based on State Law), But Could Not Be Paid By the Government	Senate
Non-Economic Damages	Proportional As to Fault	No Language	Senate
Attorney's Fees	20% Cap	No Language	Senate
Litigation	Federal Cause of Action with Consolidation	No Consolidation at Trial	House

MISCELANNEOUS: The agreement also includes language that allows victims of terrorism who have obtained a judgment against a terrorist party to access their blocked assets for satisfaction of the judgment.

SUPPLEMENTAL INFORMATION

Litigation Issues:

According to a study by the Joint Economic Committee released in May:

“...lawsuits stemming from 9/11 {are} already estimated to cost as much as \$20 billion...”

“...liability costs are estimates to constitute the largest single cost of the 9/11 attacks, and could easily exceed the property damage, life insurance, and workers compensation payments combined.”

“...such lawsuits typically pay 33 percent to 40 percent of the award to the plaintiffs’ lawyers...”

Impact on the Economy & Job Loss:

The claim that the economy has lost more than \$15 billion and 300,000 jobs in the construction industry is based on surveys conducted by the real-estate industry. The \$15 billion figure includes both estimated new construction losses and incompleting sales transactions (i.e. an individual wanted to buy an existing building, but could not secure a loan because he could not get terrorism insurance).

There is, however, disagreement on the extent of the impact of the lack of a federal terrorism reinsurance bill on the economy. CRS notes in a report for example:

“Some of the dire economic disruptions predicted in the absence of congressional agreement on a terrorism backstop have not yet become apparent. **In particular, banks have not stopped their financing for clients who lack terrorism insurance. Instead, banks are charging somewhat higher fees for some customers who are going without terrorism coverage, when there is a perception of increased risk of default as a result.**¹⁴ Lenders have not tightened credit, however, and apparently do not plan to do so for the vast majority of projects; federal bank regulators have indicated that they are not planning to put out any guidance since they have not seen any curtailment of lending.¹⁵ J. Robert Hunter, director of insurance for the Consumer Federation of America, maintains that terrorism insurance is widely available and any federal backstop should be limited to high profile buildings in New York and other major cities.¹⁶”

WHAT OTHERS ARE SAYING

Wall Street Journal Editorial *Wednesday, November 6, 2002*

A Terrifying Insurance Bill

Will Bush agree to Daschle's trial-lawyer payout?

After the elections the 107th Congress is threatening to return to pass some unfinished business, including a compromise on terrorism insurance. Having looked at the details of the insurance deal, we can only hope they'll all stay home.

The two parties have been battling for a year over this bill, especially the extent to which trial lawyers could profit from acts of terror. Republicans and some Democrats want to ban punitive damages against property owners. But Tom Daschle, carrying his usual two oceans of water for the plaintiff's bar, resisted any erosion in the right to sue the owner should a plane crash into his or her building.

And it looks like Mr. Daschle has prevailed. The compromise permits such suits, albeit before a single federal court as opposed to the more accommodating state courts. In other words, the White House appears to have caved, and after months of arguing the opposite now says terror insurance is about "jobs, not tort reform."

Well, we're not sure it's still about jobs either. The bill makes insurance companies liable for claims amounting to a certain percentage of their premiums, puts the government on the hook for 90% of losses over that deductible, and allows the government to recover some portion of its payment by levying a surcharge on all policy owners. The best news is that government help sunsets in 2005, or at least that's the promise.

Unfortunately, the bill ignores the crucial problem of risk. Risk-based premiums--which reward the careful and punish the careless--are a superb tool for reducing risk. Consider: There are lots of things property owners can do to reduce the damage from terrorism--retrofitting air-filtration systems to guard against biological agents, redesigning underground parking garages to prevent bomb attacks, fireproofing steel girders to minimize fire damage. And insurance companies can discipline them to take these measures by charging risk-based premiums.

If insurers were required to pay premiums to the government based on the premiums they receive, market incentives to reduce risk would improve markedly. If, on the other hand, terror insurance is essentially free, as it would be under the current bill, insurers have less incentive to charge the full cost of risk; instead they have every incentive to underprice it.

An alternative has been suggested by David Moss, an economist at Harvard Business School: Let the federal government pay 80% of losses from a terrorist attack, as long as insurers also pass along 80% of the premiums they collect. This way, says Mr. Moss, insurers would price risk near or at its full cost, exerting discipline against the careless, and prices would be set in the private market.

We mention Mr. Moss's idea because, despite heavy breathing by the insurance industry, it isn't at all clear that there's an immediate economic need for this legislation. It's true that right after 9/11 the property insurance market seized up. Insurers didn't know how to price for the risk of another attack, and so rent their garments that the economy would collapse without government reinsurance. We were also open to the idea, but it turns out they were wrong. The economy has continued to grow, albeit slowly, and some companies have started offering insurance again, albeit at very high premiums.

We aren't arguing that a federal backstop might not perk up business in the short term, or that some sort of insurance wouldn't be nice to have in place before another attack. But the assertion that billions of dollars of projects have been shelved and 300,000 jobs lost is bogus. Despite efforts to quantify a slowdown, including a survey by the Fed, evidence of suffering is scattered and anecdotal--and mostly confined to trophy properties.

The bigger point here is that any legislation is likely to be permanent, since no entitlement of this size has ever been allowed to ride quietly into the sunset. That argues for doing it right, and waiting until the next Congress if need be. Many Republicans are privately unhappy with the deal the White House has cut with Mr. Daschle. We hope they'll urge President Bush to insist on something better.

The Chamber of Commerce

It is vital that the Congress pass this legislation before adjourning for the year. The economy has lost more than \$15 billion and 300,000 jobs in the construction industry alone as a result of a lack of terrorism insurance coverage. We expect this legislation to provide a much needed boost to the economy, providing jobs to hundreds of thousands of workers across the country.

Although the U.S. Chamber would have preferred more extensive litigation management provisions, providing a federal cause of action and consolidation of claims has significant benefits:

- First, without this legislation, and the federal cause of action that it provides, businesses would have absolutely NO protection from predatory lawsuits that result from any future terrorist incident – they would still face forum shopping and multiple claims in state courts; courts known for rendering outrageous awards.
- Second, having these trials in federal court will provide consistent rulings, fair procedures for both plaintiffs and defendants, and provide for the use of relevant state laws that ban or otherwise limit the availability of punitive damages;
- Third, this legislation will prevent a “rush to the court-house,” which would otherwise give early lawsuit filers an advantage over later claimants; and
- Fourth, the proposal represents an improvement over the Senate bill, which did not contain consolidation for trial purposes. This provision will significantly reduce administrative and legal costs, reduce redundant, repetitive and costly discovery, and will enable both plaintiffs and defendants to deal with only one trial, rather than multiple trials with potentially inconsistent outcomes.

Of course, we would have preferred to improve the legal system even more, particularly with respect to punitive damages. However, these improvements are substantial, will add some needed momentum to the economy and are far preferable to no improvements. Ultimately we believe that this bill will improve the legal rights of both plaintiffs and defendants and, importantly will help American workers and the economy.

Considering the negative impacts on the economy that doing nothing will entail, moving a bill that backstops reinsurers and provides for exclusive federal court jurisdiction and consolidation is preferable to a continued stalemate. In short, it is the U.S. Chamber's view that this proposed solution is preferable to no action and that it should be enacted into law.
